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No. 02-1730

JUN 27 2003

IN THE

Supreme Court of the United States

BAY HARBOUR ASSOCIATES, L.P., HUNTINGTON SQUARE ASSOCIATES, L.P., ROCHESTER ASSOCIATES, L.P., VERLEYE & JERICHO ASSOCIATES, L.P. and RIVERWOOD LA PLACE ASSOCIATES, L.L.C.,

Petitioners,

v.

LEUCADIA NATIONAL CORPORATION, LEUCADIA, INC. and LUK-SHOP LLC,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF IN OPPOSITION

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COUNTER-STATEMENT OF QUESTIONS PRESENTED

1. Whether the three courts below correctly applied and interpreted well-established New York State common law contracts principles in finding that the plain language of the Agreement,[1] read as a whole, demonstrated that the parties intended the Agreement to be performed as a single integrated transaction that required the refinancing and restructuring of the Properties to be completed by an agreed upon deadline of December 15, 1999.

2. Whether the three courts below correctly found that Leucadia properly rejected Mr. Breslin's demand for a consensual foreclosure, made one day prior to the refinancing and restructuring deadline, when the Agreement permitted such demand only in furtherance of the restructuring contemplated by the Agreement, and on the date of the demand no commitment for refinancing had been obtained and the new Ventures had not been formed.

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1. All references to the agreement dated July 2, 1999 between Petitioners (sometimes referred to herein as the "Breslin Entities") and Leucadia, Inc., are made as "the Agreement."

STATEMENT PURSUANT TO RULE 29.6

Respondent Leucadia National Corporation has no parent corporation and no publicly held company owns 10% or more of its stock. Leucadia National Corporation is the direct corporate parent of Leucadia, Inc., and the indirect corporate parent of LUK-Shop, LLC. Leucadia National Corporation is the only publicly held company that owns 10% or more of Leucadia, Inc. and LUK-Shop, LLC.

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INTRODUCTION

Respondents Leucadia National Corporation, Leucadia, Inc. and LUK-Shop LLC (hereinafter, collectively, "Leucadia," except where context requires specific identification) respectfully submit that this Court should deny the Petition for a Writ of Certiorari because (1) it does not present an issue on which the circuits have issued conflicting decisions; (2) it seeks review of the court of appeals' fact-bound application of well-established state common law contracts principles; and (3) it does not present an important federal question. Rather, Petitioners devote their entire brief to the unremarkable (and incorrect) position that three lower courts misapplied well-settled New York State common law contracts principles – grounds upon which certiorari is "rarely granted." *See* Sup. Ct. R. 10.

The Second Circuit affirmed in whole the Judgment of the United States District Court for the Eastern District of New York (Hurley, J.) dated March 22, 2002, which affirmed, to the extent appealed from, the Judgment After Trial of the United States Bankruptcy Court for the Eastern District of New York State (Cyganowski, J.) dated August 4, 2002. Applying basic New York State common law contracts principles such as the parol evidence rule and reading contractual provisions in context of the entire agreement, the Bankruptcy Court completely dismissed the Breslin Entities' five-count complaint seeking, *inter alia* (i) a declaratory judgment that the agreement dated July 2, 1999 (the "Agreement") did not impose a December 15, 1999 deadline to obtain refinancing; and (ii) a declaratory judgment that Leucadia was obligated to agree to a consensual foreclosure to convey certain properties (the "Properties") to unformed Venture(s). The Bankruptcy Court granted

Leucadia's counterclaim for a declaratory judgment that the Breslin Entities' failure to obtain refinancing by the December 15, 1999 deadline entitled LUK-Shop LLC to enforce all of the rights and remedies available to it as a result of the Breslin Entities' failure to perform under the Agreement.

COUNTER-STATEMENT OF THE CASE

This adversary proceeding is a breach of contract action, nothing more, nothing less. It is not an action where the debtor seeks to assume or reject an executory contract or unexpired lease; it is not an action where the debtor seeks to enter into a post-petition contract; it is not an action to confirm a plan of reorganization. Simply stated, this breach of contract action required each of the courts below only to interpret New York State common law contracts principles, as provided in the Agreement itself. In doing so, each of the three courts below rejected the Petitioners' distorted interpretation of the Agreement, which would require that isolated provisions of the Agreement be read in a vacuum and that the full context of the Agreement, the trial testimony and other evidence in the record be ignored.

Petitioners now present a new argument to this Court based on an unsupportable and novel legal theory: that a garden variety breach of contract claim brought in an adversary proceeding should be treated as though it were a debtor's application for court approval to reject a pre-petition executory contract under the Bankruptcy Code (*see* 11 U.S.C. § 365). The obvious short-comings of such argument are highlighted further by the fact that it was the debtors who sought and obtained the Bankruptcy Court's approval to enter into the contract in the first place!

When the Agreement and the reasons why the Petitioners and Leucadia entered into it are put into context, it is readily apparent why the Petitioners' various interpretations of the Agreement have been correctly rejected by each of the courts below. Two weeks before they were about to forfeit the Properties to CFSC Capital Corp. VII ("Cargill") for failing to satisfy an agreed upon $49 million mortgage obligation, the Breslin Entities entered into the Agreement with Leucadia. The core of the Agreement provides that Leucadia would purchase from Cargill for $49 million the outstanding mortgage (the "Cargill Loans") owed by the Breslin Entities. Thereafter, the Agreement sets forth the steps of a single integrated transaction in which Leucadia would receive $34 million from a new cross-collateralized first mortgage loan obtained through to-be-formed Ventures by an agreed upon deadline of December 15, 1999. Thus, the Agreement saved the Breslin Entities from forfeiting the Properties to Cargill in July 1999 and gave them an additional six months in which to obtain financing.

The Agreement specifically states that no joint venture between Leucadia and the Breslin Entities would be formed until after the occurrence of three critical events: (i) the Venture(s) are formed; (ii) the Properties are contributed to the Venture(s); and (iii) the indebtedness under the mortgage has been restructured. (*See* Pet. 141a, § 13.)[2] The Agreement states that if refinancing and restructuring were not completed by the December 15, 1999 deadline, then Leucadia "shall be free to exercise any rights or remedies under the Cargill Loans," including foreclosing the mortgages and taking full

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2. References to the Petition for Writ of Certiorari are made as "Pet. __." References to the Joint Appendix filed in the Second Circuit are made as "A.__."

title to the Properties. (Pet. 131a, § 1.4.) The Agreement also permitted the Breslin Entities to "request that Leucadia foreclose any one or more of the Cargill Loans prior to December 15, 1999 in a consensual foreclosure *in furtherance of the restructuring contemplated under this agreement* . . . ." (*See* Pet. 131a, § 1.4) (emphasis added). The record shows, and the courts below found, that this consensual foreclosure provision was included as a "safety value" to complete the restructuring if one or more of Mr. Breslin's partners objected to the restructuring contemplated in the Agreement. (Pet. 117a-120a, 36a-37a.) There is, as the courts below found, no evidentiary or logical support for the proposition that a bald demand for a consensual foreclosure could be made as a means for the Breslin Entities to avoid the timely restructuring and refinancing required under the Agreement.

The record shows that by late October 1999 the refinancing that the Breslin Entities had hoped to secure through the to-be-formed Ventures fell through and no other potential refinancing agreements were in place. (A. 1112.) The Chief Financial Officer for the Breslin Entities admitted at trial that by that late date, it would have been "almost an impossibility" to locate a new potential lender willing to close a refinancing deal for the required sum by the December 15 deadline. (A. 730.) The record further shows that the Breslin Entities refused to restructure the Properties until after third-party refinancing was obtained through the to-be-formed Venture(s) because, if Leucadia were simultaneously a lender and an equity holder, Mr. Breslin and one or more of his partners would incur substantial tax liabilities. (A. 241, 1284-87.) Indeed, in their pre-trial brief, counsel for the Breslin Entities stated that the consensual foreclosure provision was envisioned as "a mechanism whereby, for tax reasons, the Properties would be transferred to the parties

joint venture *concurrently with obtaining the Refinancing Mortgage Loans*." (*See* A. 4, Docket Entry no. 9, Notice of Transmittal of Bankruptcy Papers to District Court, Plaintiff's Pre-trial Memorandum of Law, dated June 30, 2000, p. 15 (emphasis added).)

With the December 15, 1999 deadline looming and no refinancing agreement in place, the record shows that the Breslin Entities and their lawyers scrambled to find a solution to avoid forfeiture of the Properties, despite their failure to perform under the Agreement. (*See, e.g.*, A. 1364-366.) Mr. Breslin and his lawyers' collective attempt to devise a scheme to avoid foreclosure of the underlying mortgage and forfeiture of the Properties culminated in Mr. Breslin's demand – made one day before the December 15 refinancing and restructuring deadline – that Leucadia agree to a consensual foreclosure and a conveyance of the Properties to a non-existent Venture purportedly pursuant to section 1.4 of the Agreement. (A. 904.) The interpretation of the consensual foreclosure clause concocted by Mr. Breslin's lawyers after it became clear that the Breslin Entities would default under the Agreement would render meaningless the balance of the Agreement because a demand for a consensual foreclosure would be a substitute for the restructuring and refinancing required under the Agreement.

Recognizing the futility of the Breslin Entities' demand, Leucadia rejected it: no Venture(s) had been formed pursuant to the Agreement as of the date of the demand and no refinancing or commitments for refinancing were in place. (A. 1208.) The consensual foreclosure demanded by Breslin could not possibly be "in furtherance of the restructuring contemplated under the Agreement" without the formation of a Venture and the necessary refinancing in place.

When the December 15, 1999 deadline passed, LUK-Shop LLC was still owed approximately $34 million and, therefore, believed it could foreclose the balance of the Cargill Loans and take full title to the Properties. The Breslin Entities, however, contended that LUK-Shop LLC had to continue to wait for its $34 million and be forced to accept a 50% joint venture interest for the balance of its claim. This dispute gave rise to the present adversary proceeding.

After a four-day bench trial, the Bankruptcy Court issued a detailed 67-page Decision After Trial finding, *inter alia,* that (i) the Agreement was clear and unambiguous; (ii) all provisions of the Agreement must be read together; (iii) the Agreement set December 15, 1999 as the deadline by which the Breslin Entities were required to obtain refinancing; (iv) the Breslin Entities failed to obtain refinancing by the December 15, 1999 deadline; (v) the restructuring as contemplated by the Agreement had not come into sufficient existence to obligate Leucadia to comply with the Breslin Entities' demand for a consensual foreclosure; and (vi) as a result of the foregoing, Leucadia was entitled to exercise its rights and remedies under the Cargill Loans. (*See* Pet. 43a-121a.) Judge Cyganowski, the trial court judge, found all the witnesses at trial – *except* Mr. Wilbur Breslin (the Breslin Entities' principal) – to be credible, and described as "schizophrenic" the Breslin Entities' arguments that Leucadia somehow breached the Agreement and must consent to a foreclosure of the Properties to a non-existent Venture. (*See* Pet. 107a, 114a.) Judge Cyganowski also found that Mr. Breslin's own conduct and the conduct of the Breslin Entities' attorneys discredited the Breslin Entities' specious argument that December 15, 1999 was not a deadline to obtain refinancing. (Pet. 73a-74a.)

The Breslin Entities limited their appeal to the District Court primarily to the issue of whether Leucadia had the right to reject the Breslin Entities' demand for consensual foreclosure. (*See* Pet. 26a.) The District Court affirmed the Decision and Judgment of the Bankruptcy Court and expressly rejected the Breslin Entities' argument that Leucadia was required to agree to Mr. Breslin's demand for a consensual foreclosure, finding "that the consensual foreclosure language must be considered in conjunction with the verbiage which immediately follows, viz., 'in furtherance of the restructuring contemplated under this agreement.'" (Pet. 32a.) The Second Circuit affirmed in whole the District Court's Judgment, and denied the Breslin Entities' petition for a panel rehearing. (Pet. 1a and 3a.)

REASONS FOR DENYING THE PETITION

In their attempt to have this Court grant certiorari, Petitioners propose a novel application of Chapter 11 bankruptcy principles to garden variety breach of contract actions interpreted under state common law. The thrust of Petitioners' newly-minted argument is that courts should apply a pro-debtor gloss when presented with "two reasonable but conflicting interpretations" of an unambiguous contract. (Pet. i.) Petitioners hope that this Court will adopt this novel approach to interpret all contracts "entered into with the imprimatur of the Bankruptcy Court as blueprints for reorganization." (Pet. 6.) Petitioners argue for the first time in this action that "Chapter 11's purpose of rehabilitating the Petitioners" should prevail over the straightforward analysis of whether the Breslin Entities failed to satisfy their contractual obligations under an agreement governed by New York State law. (Pet. 4.)

It is respectfully submitted that the Petition for a Writ of Certiorari should be denied because the lower courts properly interpreted the Agreement under well-established state common law principles without the novel gloss proposed by Petitioner. Each of the three lower courts correctly rejected the Breslin Entities' interpretation of the Agreement as contrary to fundamental contracts law, which requires the parties' intent to be discerned by reading the contract as a whole, and by considering all its clauses together and in context to determine if and to what extent one may modify, explain or limit another. (Pet. 116a-117a (Bankruptcy Court), 31a-32a (District Court), 8a (Second Circuit).) Indeed, the evidentiary record weighs so heavily against the Breslin Entities' after-the-fact interpretations of the Agreement that their briefs to the lower courts and to this Court fail to cite to any portion of the record to support their bald conclusions, the ludicrous straw man arguments that they incorrectly attribute to Leucadia or "findings" that they incorrectly attribute to the courts below.

THE SECOND CIRCUIT CORRECTLY APPLIED WELL ESTABLISHED COMMON LAW CONTRACTS PRINCIPLES TO AFFIRM THE DISTRICT COURT'S JUDGMENT

The Second Circuit correctly saw this dispute for what it is – a garden variety breach of contract action. (Pet. 7a.) In doing so, the Second Circuit gave short-shrift to the Petitioners' interpretations of the Agreement and applied well-established common law contracts principles to find that "under the agreement, read as a whole, the Debtors had no right to consensual foreclosure absent new financing, and because the deadline had passed, Leucadia was free to pursue any remedies available to it under the notes it had purchased."

(Pet. 8a.) (citing *Mastrobuono v. Shearson Lehman Hutton, Inc.*, 514 U.S. 52, 63 (1995) and *Kinek v. Paramount Communs., Inc.*, 22 F.3d 503, 509 (2d Cir. 1994)).

Failing to find any relevant authority to support their novel argument that the lower courts should have applied some sort of Bankruptcy Code gloss to their interpretation of a contract governed by New York State law, Petitioners instead rely on *NLRB v. Bildisco & Bildisco*, 465 U.S. 513, 104 S. Ct. 1188 (1984).

Petitioners' reliance on *Bildisco* is completely misplaced. In *Bildisco*, this Court examined two questions not even remotely related to any of the issues in this action:

> (1) under what conditions can a Bankruptcy Court permit a debtor-in-possession to reject a collective-bargaining agreement; (2) may the National Labor Relations Board find a debtor in-possession guilty of an unfair labor practice for unilaterally terminating or modifying a collective-bargaining agreement before rejection of that agreement has been approved by the Bankruptcy Court.

Bildisco, 465 U.S. at 516, 104 S. Ct. at 1191. In deciding those questions, this Court held that the phrase "executory contract" in 11 U.S.C. § 365 of the Bankruptcy Code includes collective-bargaining agreements subject to the National Labor Relations Act, and that the Bankruptcy Court may approve rejection of such contracts by the debtor-in-possession upon an appropriate showing. *Id.* at 516, 104 S. Ct. at 1191. This Court further held that, because of the special nature of a collective-bargaining contract, and the

consequent "law of the shop" that it creates, the Bankruptcy Court should apply a "somewhat stricter standard" in deciding whether to allow a debtor-in-possession to reject such an agreement. *Id.* at 523-24, 104 S. Ct. at 1195. The Court reasoned that, since "the policy of Chapter 11 is to permit successful rehabilitation of debtors, rejection should not be permitted without a finding that that policy would be served by such action." *Id.* at 527, 104 S. Ct. at 1196. The present case, however, does not involve approval of a debtor's rejection of a pre-petition executory contract.

In relying on *Bildisco* to support their novel legal theory, Petitioners have confused two strikingly different legal concepts: a debtor seeking court approval to reject a pre-petition executory contract to preserve its estate (*see* 11 U.S.C. § 365) *versus* a debtor breaching a court-approved post-petition contract by failing to perform its contractual obligations. Petitioners' attempt to apply Bankruptcy Code principles relating to pre-petition obligations to post-petition court-approved contracts is contrary to the case law interpreting the Bankruptcy Code. For example, in *In re Embrace Systems Corp.*, 178 B.R. 112, 122 (W.D. Mich. 1995), the Court refused to apply Section 365 to a postpetition contract, stating: "Section 365 does not govern the standards by which a debtor may enter into *new* contracts postpetition; rather, it sets forth requirements for a debtor to either assume or reject a contract that was already in existence prepetition and has not yet expired." *Id.* at 122 (italics in original).

In the present case, Petitioners sought and received permission from the Bankruptcy Court to enter into the post-petition Agreement with Leucadia. By entering into the Agreement, Petitioners avoided defaulting on their debt and

forfeiting their property to Cargill. The Agreement with Leucadia therefore gave Petitioners a second chance to obtain financing to avoid forfeiting their property.

Petitioners' argument that the Bankruptcy Court failed to give effect to Chapter 11's purpose of rehabilitating the Petitioners is belied by the record. When Petitioners sought the Bankruptcy Court's approval to enter into the Agreement, counsel for the Petitioners explained to the Court: "This agreement sets up the preliminary financing and then it provides a vehicle for the further financing which would be the financing that would take the debtors out of the bankruptcy proceeding." (A. 1557.) After counsel for Petitioners explained the details of the Agreement to the Court, the Petitioners were authorized to enter into the Agreement. (A. 1585, 1540-1542.) Accordingly, the Bankruptcy Court's order approving the Agreement promoted the Petitioners' attempt to rehabilitate and to reorganize.

By applying New York law (which governs the Agreement, *see* Pet. 140a, § 11), the courts below properly enforced the terms of the very agreement that the Petitioners sought and received permission to enter into. There is no policy reason to permit debtors to breach post-petition court-approved contracts. Indeed, quite the opposite is true: If post-petition contracts were to be interpreted in the manner suggested by Petitioners, third-parties would be disinclined to enter into them and that would obviously not promote the reorganization policy.

CONCLUSION

For the reasons set forth above, the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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